

G. Customer Risk. Each insured depository institution shall develop and implement a written due diligence process that:

1. Identifies customers, including fund providers, fund takers, and capital market/asset management counterparties, that represent material risk exposure to the institution;
2. Evaluates their Year 2000 preparedness;
3. Assesses their existing and potential Year 2000 risk to the institution; and
4. Implements appropriate risk controls, including controls for underwriting risk, to manage and mitigate their Year 2000 risk to the institution.

H. Involvement of the Board of Directors and Management.

1. During all stages of the renovation, testing, and contingency planning process, the board of directors and management of each insured depository institution shall:

- a. be actively involved in efforts to plan, allocate resources, and monitor progress towards attaining Year 2000 readiness;
- b. oversee the efforts of the insured depository institution to achieve Year 2000 readiness and allocate sufficient resources to resolve problems relating to the institution's Year 2000 readiness; and
- c. evaluate the Year 2000 risk associated with any strategic business initiatives contemplated by the insured depository institution, including mergers and acquisitions, major systems development, corporate alliances, and system interdependencies.

2. In addition, the board of directors, at a minimum, shall require from management, and management shall provide to the board of directors, written status reports, at least quarterly and as otherwise appropriate to keep the directorate fully informed, of the insured depository institution's efforts in achieving Year 2000 readiness. Such written status reports shall, at a minimum, include:

- a. The overall progress of the insured depository institution's efforts in achieving Year 2000 readiness;
- b. The insured depository institution's interim progress in renovating, validating, and contingency planning measured against the insured depository institution's Year 2000 project plan as adopted under section II.A.5. of appendix B;
- c. The status of efforts by key external third party suppliers and other material third parties in achieving Year 2000 readiness;
- d. The results of the testing process;
- e. The status of contingency planning efforts; and
- f. The status of the ongoing assessment of customer risk.

[64 FR 66704, 66706, Nov. 29, 1999]

PART 365—REAL ESTATE LENDING STANDARDS

Sec.

365.1 Purpose and scope.

365.2 Real estate lending standards.

APPENDIX A TO PART 365—INTERAGENCY GUIDELINES FOR REAL ESTATE LENDING POLICIES

AUTHORITY: 12 U.S.C. 1828(o).

SOURCE: 57 FR 62896, 62900, Dec. 31, 1992, unless otherwise noted.

§ 365.1 Purpose and scope.

This part, issued pursuant to section 304 of the Federal Deposit Insurance Corporation Improvement Act of 1991, 12 U.S.C. 1828(o), prescribes standards for real estate lending to be used by insured state nonmember banks (including state-licensed insured branches of foreign banks) in adopting internal real estate lending policies.

§ 365.2 Real estate lending standards.

(a) Each insured state nonmember bank shall adopt and maintain written policies that establish appropriate limits and standards for extensions of credit that are secured by liens on or interests in real estate, or that are made for the purpose of financing permanent improvements to real estate.

(b)(1) Real estate lending policies adopted pursuant to this section must:

(i) Be consistent with safe and sound banking practices;

(ii) Be appropriate to the size of the institution and the nature and scope of its operations; and

(iii) Be reviewed and approved by the bank's board of directors at least annually.

(2) The lending policies must establish:

(i) Loan portfolio diversification standards;

(ii) Prudent underwriting standards, including loan-to-value limits, that are clear and measurable;

(iii) Loan administration procedures for the bank's real estate portfolio; and

(iv) Documentation, approval, and reporting requirements to monitor compliance with the bank's real estate lending policies.

(c) Each insured state nonmember bank must monitor conditions in the real estate market in its lending area

to ensure that its real estate lending policies continue to be appropriate for current market conditions.

(d) The real estate lending policies adopted pursuant to this section should reflect consideration of the Interagency Guidelines for Real Estate Lending Policies established by the Federal bank and thrift supervisory agencies.

APPENDIX A TO PART 365—INTERAGENCY GUIDELINES FOR REAL ESTATE LENDING POLICIES

The agencies' regulations require that each insured depository institution adopt and maintain a written policy that establishes appropriate limits and standards for all extensions of credit that are secured by liens on or interests in real estate or made for the purpose of financing the construction of a building or other improvements.⁵ These guidelines are intended to assist institutions in the formulation and maintenance of a real estate lending policy that is appropriate to the size of the institution and the nature and scope of its individual operations, as well as satisfies the requirements of the regulation.

Each institution's policies must be comprehensive, and consistent with safe and sound lending practices, and must ensure that the institution operates within limits and according to standards that are reviewed and approved at least annually by the board of directors. Real estate lending is an integral part of many institutions' business plans and, when undertaken in a prudent manner, will not be subject to examiner criticism.

LOAN PORTFOLIO MANAGEMENT CONSIDERATIONS

The lending policy should contain a general outline of the scope and distribution of the institution's credit facilities and the manner in which real estate loans are made, serviced, and collected. In particular, the institution's policies on real estate lending should:

- Identify the geographic areas in which the institution will consider lending.
- Establish a loan portfolio diversification policy and set limits for real estate loans by type and geographic market (e.g., limits on higher risk loans).
- Identify appropriate terms and conditions by type of real estate loan.

⁵The agencies have adopted a uniform rule on real estate lending. See 12 CFR part 365 (FDIC); 12 CFR part 208, subpart C (FRB); 12 CFR part 34, subpart D (OCC); and 12 CFR 563.100–101 (OTS).

- Establish loan origination and approval procedures, both generally and by size and type of loan.

- Establish prudent underwriting standards that are clear and measurable, including loan-to-value limits, that are consistent with these supervisory guidelines.

- Establish review and approval procedures for exception loans, including loans with loan-to-value percentages in excess of supervisory limits.

- Establish loan administration procedures, including documentation, disbursement, collateral inspection, collection, and loan review.

- Establish real estate appraisal and evaluation programs.

- Require that management monitor the loan portfolio and provide timely and adequate reports to the board of directors.

The institution should consider both internal and external factors in the formulation of its loan policies and strategic plan. Factors that should be considered include:

- The size and financial condition of the institution.
- The expertise and size of the lending staff.
- The need to avoid undue concentrations of risk.
- Compliance with all real estate related laws and regulations, including the Community Reinvestment Act, anti-discrimination laws, and for savings associations, the Qualified Thrift Lender test.
- Market conditions.

The institution should monitor conditions in the real estate markets in its lending area so that it can react quickly to changes in market conditions that are relevant to its lending decisions. Market supply and demand factors that should be considered include:

- Demographic indicators, including population and employment trends.
- Zoning requirements.
- Current and projected vacancy, construction, and absorption rates.
- Current and projected lease terms, rental rates, and sales prices, including concessions.
- Current and projected operating expenses for different types of projects.
- Economic indicators, including trends and diversification of the lending area.
- Valuation trends, including discount and direct capitalization rates.

UNDERWRITING STANDARDS

Prudently underwritten real estate loans should reflect all relevant credit factors, including:

- The capacity of the borrower, or income from the underlying property, to adequately service the debt.
- The value of the mortgaged property.